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IN THE

Supreme Court of the United States

OCTOBER TERM, 1959.

No. 589

GERTRUDE A. FARNSWORTH, JAMES D. CARPENTER, and ROBERT M. SHARPE, Executors under the Will of DANIEL W. FARNSWORTH and GERTRUDE A. FARNSWORTH,

Petitioners,

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

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MILTON A. DAFBER,
On the Petition.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1959.

No.

GERTRUDE A. FARNSWORTH, JAMES D. CARPENTER, and ROBERT M. SHARPE, Executors under the Will of DANIEL W. FARNSWORTH, and GERTRUDE A. FARNSWORTH,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

The undersigned counsel for petitioners prays that a Writ of Certiorari issue to review the judgment of the United States Court of Appeals entered in the above case on October 9, 1959.

Opinions Below.

The opinion of the Tax Court of the United States (R. 47a) is reported at 29 T. C. 1131 (1958). The opinion of the Court of Appeals for the Third Circuit is reported at 270 F. 2d 660 (3d Cir. 1959), and is appended to this petition at pages A-3 ff.

Jurisdiction.

The judgments of the Court of Appeals for the Third Circuit were made and entered on October 9, 1959, and copies thereof are appended to this petition at pages A-1 ff. The jurisdiction of this Court is invoked under 28 U. S. C. 1254(1).

Questions Presented.

This is a Federal Income Tax case. Decedent Daniel W. Farnsworth claimed deductions in his income tax returns for 1952 and 1953 for unincorporated business taxes which he paid, and which were imposed by the State of New York against the partnership of Farnsworth & Farnsworth of which he was senior partner. The State of New York had entered a judgment against him in New York for the full amount of the taxes and against his partners for their share of the taxes for the years in which they were members of the firm. Farnsworth, who was still in business in New York, paid those New York taxes in full during the two years under review and deducted them pursuant to the express provision of the Internal Revenue Code of 1939. The Tax Court, holding that he was liable for only that part of the New York taxes measured by his proportionate interest in the partnership, disallowed all but a small part of the deduction. The Court of Appeals for the Third Circuit affirmed.

The questions presented are:

1. Whether a taxpayer who is by judgment liable for the full amount of state taxes imposed upon a partnership of which he is a member may deduct the actual amount of such state taxes directly and personally paid by him.

2. Whether a cash basis taxpayer may be deprived of a deduction for state taxes assessed upon and paid by him because of an alleged right to contribution from others.

Statutes and Regulations Involved.

The pertinent portions of the Internal Revenue Code of 1939 and of Treasury Regulations 118 adopted pursuant thereto are appended to this petition at pages A-13 ff.

Statement.

During the years 1940 through 1949, Daniel W. Farnsworth and others were members of a series of partnerships under the name of Farnsworth & Farnsworth. While the business of this firm was continuous over the period, partnership agreements were signed annually, and both the membership in the firm and the percentage interests of the partners changed from year to year (R. 48a-49a).

These partnerships were formed under the laws of New Jersey, inasmuch as most of the members were New Jersey residents and the firm maintained an office and carried on some of its activities in New Jersey. During the 1940's the firm filed returns under Article 16 A of the New York Tax Law and allocated its business income between New York and New Jersey. The New York Unincorporated Business taxes shown due by these returns with respect to income allocated to New York were paid and are not in issue here (R. 50a).

In 1951, the New York Tax Commission examined these returns and determined that in fact no income was properly allocable to New Jersey, and that the firm should have paid New York Unincorporated Business Tax with respect to its entire business income, rather than merely an allo-

cable part thereof. Accordingly, the New York Tax Commission assessed deficiencies, and as well interest and penalties, against the firm (R. 62a-63a).

Conformably to New York law the Commission filed warrants of judgment in the office of the Clerk of New York County against Daniel W. Farnsworth for the entire amount assessed, and against each of his partners or former partners for the entire amount assessed with respect to the years during which they were members of the firm (R. 63a).

The total amount of these assessments was $143,388.61. The reason they were filed against Daniel W. Farnsworth in the full amount was that he had been a member of the firm during all of the years involved and under New York law each member of the firm is both jointly and severally liable for all obligations of the firm, and his separate property is subject to levy for firm debts without prior recourse to firm assets. In short, under New York law Farnsworth individually was primarily liable for the entire Unincorporated Business Tax.

When the assessments were made, and the warrants filed, Farnsworth engaged counsel, who entered into settlement negotiations with the New York Tax Commission. The Tax Commission refused to settle unless all of the partners joined in and unless the settlement disposed of all related tax issues (R. 52a, 78a-79a). This demand could not be met, however, because other partners or former partners in Farnsworth & Farnsworth denied any liability to New York and engaged their own counsel to resist the New York deficiency assessment, rather than compromise it (R. 69a-70a, 95a).

In April, 1952, Farnsworth called a meeting of his partners and former partners at his home in Montclair, New Jersey. At this meeting he offered to bear the entire burden

of the deficiencies if the other partners would "cooperate" in achieving a settlement (R. 52a, 80a). This offer was accepted by his partners, either expressly at the meeting or by their subsequent conduct (R. 69a-70a, 99a-100a). Farnsworth's counsel, with the cooperation of counsel for the other partners, resumed negotiations with the New York authorities, and a settlement agreement was finally executed in November, 1952 (R. 63a). As a part of their cooperation in effecting this settlement, the other partners, on demand of the State Tax Commission, each executed a confession of judgment for the entire amount of taxes, interest and penalties assessed against him with respect to the years when he was a member of the firm, which confession was to be usable against him within or without New York if there should be any default in performance of the settlement terms (R. 62a, 64a). Since most of the partners neither resided, did business, nor had property within New York, and were therefore substantially immune from New York enforcement machinery, the concession thus made by them was substantial.

The settlement agreement was highly beneficial. Under it the Commission waived penalties entirely (R. 52a). In addition, provision was made for payment of the agreed deficiency in tax over a period of three years. The testimony of Farnsworth showed that this reduction in liability, and provision for installment payment, saved him and his business from ruin (R. 71a).

Inasmuch as his partners had lived up to their end of the bargain by cooperating in working out a settlement, and securing same by their individual confessions of judgment, Farnsworth honored his obligation to them. In 1952 he personally paid to New York the sum of $31,153.98, representing the total amount of unincorporated business

tax deficiency payable in 1952 pursuant to the settlement (R. 53a). In 1953, similarly, he paid the sum of $19,488.25, representing the amount of unincorporated business tax, and interest thereon, required to be paid in 1953 (R. 53a).

In his Federal income tax returns for the years 1952 and 1953 Farnsworth claimed deductions for the amounts so paid. Mr. Farnsworth was a cash basis taxpayer, and he denominated these items as interest and state taxes paid within the taxable year. In each case the claimed deduction was disallowed, except to the extent of Farnsworth's average percentage of interest in the profits of the firm during the ten years to which the New York taxes related.

Reasons for Granting a Writ.

The decision below should be reviewed and reversed because it erroneously interprets the provisions of the Internal Revenue Code of 1939, which have been carried over substantially unchanged into the Internal Revenue Code of 1954, so as to disrupt the orderly and efficient administration of the Internal Revenue laws. The question presented, dealing with the deductibility of local taxes actually paid by a cash basis taxpayer in the case of a partnership, is equally applicable to any situation where a number of persons are jointly and severally liable for a local tax, *e. g.*, in the case of real property owned by tenants in common. The questions are, therefore, of far-reaching importance in the administration of the Revenue laws.

In addition, the decision of the Court of Appeals for the Third Circuit conflicts in principle with the decisions of the First Circuit in *Flood* v. *United States*, 133 F. 2d 173 (1st Cir. 1943), and of the Sixth Circuit in *Siarto* v. *Commissioner*, 171 F. 2d 293 (6th Cir. 1948) and *Hord* v. *Commissioner*, 95 F. 2d 179 (6th Cir. 1938).

Finally, the decision of the Third Circuit erroneously interprets and distorts the meaning of this Court's decision in *Magruder v. Supplee*, 316 U. S. 394 (1942).

1. The New York State Unincorporated Business Tax is imposed upon the net income of every person or partnership doing business in the State of New York. *McKinney's New York Tax Law*, Section 386(a). The New York statute contains no specific provision for enforcement against a partnership as such. But the proceedings taken in the instant case show clearly the administrative construction adopted by the New York Tax Commission with regard to enforcement against partnerships and partners. The judgment warrants were filed not merely against the firm in its own name, but as well against the several partners "individually and as co-partners" for the full amount of the tax (R. 62a). And by the terms of the settlement agreement the State Tax Commission required Daniel W. Farnsworth to acknowledge individual liability for the whole amount of the unincorporated business tax (Appendix A-20 ff.). In short, the administrative construction of Article 16A of the New York Tax Law shows clearly that each individual partner is primarily and severally liable for the entire tax indebtedness of the firm.

And enforcement of unincorporated business tax liabilities in this manner is in accordance with New York law dealing with the general liability of a partner for firm debts. In the substantive sense, the firm's debt is several as well as joint and can be enforced against any partner properly served, without prior recourse to the firm's property.

In *Patrickes v. J. H. C. Service Station*, 180 Misc. 197, 41 N. Y. S. 2d 158 (N. Y. City Ct. 1943), *aff'd per curiam* 180 Misc. 927, 46 N. Y. S. 2d 233 (Sup. Ct. App. Term, 2d Dept. 1943), the entire question of the character and extent

of the partner's individual liability for firm obligations was exhaustively analyzed. The Court stated that an absolute liability rests on each partner for the whole amount of the firm debt; and that, although originally a joint obligation, it may be several as to its effects. What is more, the Court stated that the individual liability of each partner dates back to the time when the obligation was incurred and arises simultaneously with the partner's joint liability; and that, with respect to the ultimate rights of creditors, the contractual obligations of a partnership are incurred by all and as well by each partner. Similarly, it has been held that the creditor upon a joint obligation of a partnership may make execution at will out of either the partnership property or the property of the individual partners who have been served with process; and that the lien of a judgment against the firm becomes a lien on the individual property of each partner to the same extent as though the judgment were based upon an individual debt. *Gómez v. Vasquez*, 177 Misc. 874, 32 N. Y. S. 2d 34 (N. Y. City Ct., Special Term 1941).

These decisions, rendered under the Uniform Partnership Act, implement principles which had been announced by the New York Court of Appeals at an earlier date, and with respect primarily to the common law. The most concise statement of the character of a partner's liability for the joint obligations of the firm is set forth in *People v. Knapp*, 206 N. Y. 373, 99 N. E. 841 (1912):

> "The promise of a copartnership is joint as to all the members and several as to each. As between the partners themselves the assets are marshaled in equity so that joint assets are first used in the payment of joint debts and several assets in the payment of several debts. This rule, however, does not bind creditors who may select any partner and collect

their claims wholly from the property of that partner. Therefore, when the trust company made a loan to the firm of Knapp Bros., all the members of the firm became liable jointly, and each member thereof became liable severally to pay the debt. Regardless of the form of the transaction, the loan was made to all and to each in the theory of law. * * * "

And see *Seligman* v. *Friedlander*, 199 N. Y. 373, 92 N. E. 1047 (1910); *Caplan* v. *Caplan*, 268 N. Y. 445, 198 N. E. 23 (1935).

Since Farnsworth was personally and primarily liable for the whole amount of the unincorporated business taxes assessed against the firm, there should be no doubt of his right to deduct the same when he actually paid them. Repeated decisions of the Tax Court, the Board of Tax Appeals, the Courts of Appeal, and the Commissioner of Internal Revenue himself, prior to the instant case, amply sustain this deduction. *Al Jolson*, 3 T. C. 1184 (1944); *Robert C. Liggett*, 4 T. C. M. 598 (1945); *F. C. Nicodemus, Jr.*, 26 B. T. A. 125 (1932); *Thomas D. Conroy*, 17 T. C. M. 21 (1958); G. C. M. 15,530, XIV-2 C. B. 107 (1935); G. C. M. 17,570, 1937-1 C. B. 193; *Estate of John Edgerly Morrill*, 43 B. T. A. 651 (1941); *Cornelia C. F. Horseford*, 2 T. C. 826 (1943).

In the instant case, however, deductibility was denied upon a finding that Mr. Farnsworth had gratuitously waived a right of contribution from his partners with respect to what would otherwise have been their *pro rata* shares of these taxes. In so ruling, the Court of Appeals overlooked basic and well-fixed principles of tax accounting, which are necessary to an orderly and efficient administration of the Revenue laws. The deductibility of taxes actually paid by a party primarily liable for the same is provided by

Section 23(c)(1) of the Internal Revenue Code of 1939 and its successor, Section 164 of the Internal Revenue Code of 1954. Neither Section suggests that a right of contribution affects deductibility. And this for the reason that tax consequences arising from the existence of a right of contribution are to be determined upon quite different principles.

If Farnsworth had ever collected upon his right of contribution against the others, then the monies so collected would have been gross income taxable to him in the year of recovery. *Burnet* v. *Sanford & Brooks Co.*, 282 U. S. 359 (1931); *Lloyd H. Faidley*, 8 T. C. 1170 (1947). But, in fact, he did not collect anything from the others. Instead, in order to induce the others to join in a settlement with New York State, Farnsworth waived his right of contribution. Since this waiver was granted in a business transaction, perhaps the other partners sustained taxable income themselves in 1952 by reason of cancellation of indebtedness. If so, the proper tax treatment would be to make assessments against the other partners, not against Mr. Farnsworth. On the other hand, if a gift had been intended, then the proper procedure would be to assess Farnsworth for a gift tax as provided for under Section 1000 *et seq.* of the Internal Revenue Code of 1939, and not to assess Mr. Farnsworth for additional income tax.

Orderly and efficient administration of the income tax law requires meticulous adherence by the Commissioner to the principles of law and of tax accounting which have been dictated by statute, and which, over the years, have become firmly embedded in the tax structure. Patently, what has occurred in the instant case is an attempt by the Commissioner to increase the revenue improperly, through disallowing deductions to Farnsworth which are expressly per-

mitted in Section 23(c)(1) of the Internal Revenue Code of 1939.

The case merits attention by this Court not because of an individual injustice, but rather because the principle here applied will operate to deny a well-settled right of deduction to countless taxpayers who, relying on the Commissioner's own prior rulings, and upon the decisions of the Courts, have taken deductions for taxes which they themselves have paid, notwithstanding that others were concurrently liable. The effect of the present decision may well be to encourage the Commissioner to impose deficiency assessments with regard to such taxpayers, not only for future years, but as well with respect to returns heretofore filed for taxable years ended as long ago as December 31, 1956.

There can be no doubt that the problems discussed above are of great and recurring significance in the administration of the Internal Revenue laws. The legal principles and statutory provisions of the Internal Revenue Code of 1939 which affect this case have been carried over substantially unchanged in principle (although modified in detail) in the Internal Revenue Code of 1954. Latest available statistics show that during 1957 almost two million individual taxpayers made returns showing profit or loss from partnerships, involving a total of 9.9 billion dollars in reported taxable income and 604 million dollars in claimed net losses. In addition, although we do not know the extent to which taxpayers making returns are owners in common of property, the statistics do disclose that five and one-half million taxpayers filed returns showing income or loss from rents or royalties, involving 3.9 billion dollars of taxable income from this source and 680 million dollars of claimed losses. See *Statistics of Income—1957, Individual Income Tax*

Returns, I. R. S. Pub. No. 79 (1959), at 22. Certainly, in every case in which the income-producing property involved was held in common, or in entirety by husband and wife filing separate returns, the problem of deductibility for taxes presented by the *Farnsworth* case will be involved. This would include, in practical effect, a great many cases of inheritors of real property.

The decision below erroneously interprets this Court's decision in *Magruder* v. *Supplee*, *supra*. In *Magruder* v. *Supplee*, the taxpayer purchased real property during the middle of the year. Under local law the real estate tax continued to be a lien upon the land and the seller made allowance in the price for the unpaid portion of the tax. The purchaser thereafter sought to deduct the amount so allowed. This Court held that the deduction was not authorized for the reason that the tax was imposed upon the vendor rather than the purchaser, and that Section 23(c)(1) did not permit the deduction for taxes paid except by the person upon whom assessed.*

In view of the fact that under New York law Mr. Farnsworth was at all times personally liable, primarily and severally, for the entire unincorporated business tax, there can be no doubt that he was the person upon whom the taxes were assessed. Consequently, his right to deduction should have been unquestioned. The extension of the *Supplee* doctrine to the instant case will seriously affect previously well-established principles as to the effect of local law in determining the identity of a person upon whom local taxes are assessed and to that extent it will disrupt the orderly administration of the Federal Income Tax law.

The decision of the Court of Appeals in this case is contrary to principles established by prior decisions of other

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* The rule of the *Supplee* case has been changed by statute, § 164(d), Internal Revenue Code of 1954.

Circuits dealing with analogous situations. In *Hord* v. *Commissioner, supra,* the taxpayer, a beneficiary, paid a local property tax which had previously been assessed against the trustee of a trust. In allowing the deduction to Mr. Hord the Sixth Circuit held that he was at least secondarily liable for the tax under Ohio law and that, therefore, in paying the tax he discharged his own tax obligation. The instant case, by contrast, has denied the deduction to Mr. Farnsworth even though he was primarily liable for the tax.

In *Siarto* v. *Commissioner, supra,* the Sixth Circuit in a *per curiam* opinion affirmed a decision of the Tax Court which allowed one partner to deduct the entire amount of a partnership business expense which he had unilaterally undertaken to pay. The Court here treated the transaction as in substance and effect a modification of the partnership agreement. In the instant case, by contrast, even in the face of the express modification of the partnership agreement, the Tax Court and the Third Circuit denied Farnsworth a deduction for a partnership expense which had been allocated to him in its entirety.

In *Flood* v. *Commissioner, supra,* the First Circuit allowed deductions for business expenses paid by partners after the termination of the firm. Here, by contrast, payment of a proper business expense, *i.e.,* a local tax assessed retroactively after several partnership years had ended, was disallowed.

It is true that none of the three cited cases are exactly like the one at bar; all of them exhibit slight divergencies in fact. Nonetheless, the principles of law which are implicit (though scarcely expressed) in the opinion of the Third Circuit are inconsistent with the principles embodied and expressed in the cited decisions. A conflict of Circuits as to basic principle is as disruptive as is a conflict upon

precisely identical facts, and requires clarification and determination by this Court.

The instant decision is further inconsistent in principle with the decision of the First Circuit in *Flood* v. *Commissioner, supra,* insofar as it relates to the general rules applicable to taxation of partnerships. It is perfectly clear that the basic pattern of Federal income taxation with regard to partners and partnerships both under the 1939 Code (§181 *et seq.*) and under the 1954 Code (§701 *et seq.*) is to treat the firm as a mere aggregation of individuals. For example, it is and was substantially provided that the partner, and not the partnership, is subject to tax and that each partner must take into account in computing his own income tax all of the different classes of income and the deduction which arises from the operation of the firm. And such things as the percentage limitations upon deductions, and the character of the net gain or loss from the sale of property used in the trade or business, are determined separately by each partner through aggregation of his individual transactions with his aliquot share of the firm's transactions, rather than solely by reference to the operations of the firm itself. As was justly said by the First Circuit in the *Flood* case, "the partnership is merely a skin deep accounting entity; it is not in any sense a taxable entity".

The Third Circuit in the instant case has adopted a radically different theory of the partnership. The Third Circuit and the Tax Court have treated the partnership as a taxable entity by ruling that the "liability" for unincorporated business tax is that of the partnership itself and that, therefore, the payment of these taxes by Farnsworth must be treated as a contribution to the firm, rather than as the payment of a tax for which he himself was liable.

The so-called "entity" theory of partnership adopted by the Courts below, is not only inconsistent with the plain language of the Internal Revenue Codes of 1939 and of 1954, but as well violates the general principles of partnership law which are in effect throughout the Anglo-Saxon world. As pointed out above, in New York, and as well in virtually every jurisdiction of common law background, the accurate characterization of a partnership debt is solely and simply that it is a joint and several obligation of each partner. Congress has recognized these legal principles and made them applicable in determination of the tax consequences of doing business in the partnership form. This Court should grant certiorari and reaffirm the plainly indicated Congressional intention that deductibility of items of partnership expense is to be determined by reference to the partners who actually pay the same, and who are primarily liable for the same in their several capacities, rather than by reference to the partnership itself as an entity.

Conclusion.

For the reasons set forth above, it is respectfully submitted that this petition for a writ of certiorari should be granted.

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MILTON A. DAUBER,
On the Petition.

APPENDIX.

I.

Judgment of U. S. Court of Appeals, Third Circuit.

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT.

No. 12,703.

GERTRUDE A. FARNSWORTH and GERTRUDE ADAMS FARNSWORTH, JAMES D. CARPENTER and ROBERT M. SHARPE, Executors of the Last Will and Testament of DANIEL WILLIAMS FARNSWORTH, Deceased,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

(Tax Court No. 60596.)

ON PETITION TO REVIEW A DECISION OF THE TAX COURT OF THE UNITED STATES.

Present: BIGGS, Chief Judge, and MCLAUGHLIN and HASTIE, Circuit Judges.

Judgment.

This cause came on to be heard on the record from the Tax Court of the United States, and was argued by counsel.

On consideration whereof, it is now here ordered, adjudged and decreed by this Court that the decision of the said Tax Court in this cause be, and the same is hereby affirmed.

Attest:

IDA O. CRESKOFF,
Clerk.

October 9, 1959.

Judgment of U. S. Court of Appeals, Third Circuit.

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT.

No. 12,704.

GERTRUDE A. FARNSWORTH and GERTRUDE ADAMS FARNSWORTH, JAMES D. CARPENTER and ROBERT M. SHARPE, Executors of the Last Will and Testament of DANIEL WILLIAMS FARNSWORTH, Deceased,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

(Tax Court No. 64736.)

ON PETITION TO REVIEW A DECISION OF THE TAX COURT OF THE UNITED STATES.

Present: BIGGS, Chief Judge, and McLAUGHLIN and HASTIE, Circuit Judges.

Judgment.

This cause came on to be heard on the record from the Tax Court of the United States, and was argued by counsel.

On consideration whereof, it is now here ordered, adjudged and decreed by this Court that the decision of the said Tax Court in this cause be, and the same is hereby affirmed.

Attest:

Clerk.

October 9, 1959.

II.

Opinion of U. S. Court of Appeals, Third Circuit.

(Filed October 9, 1959)

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

No. 12,703

GERTRUDE A. FARNSWORTH AND GERTRUDE ADAMS FARNSWORTH, JAMES D. CARPENTER AND ROBERT M. SHARPE, Executors of the Last Will and Testament of DANIEL WILLIAMS FARNSWORTH, Deceased,

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GERTRUDE A. FARNSWORTH AND GERTRUDE ADAMS FARNSWORTH, JAMES D. CARPENTER AND ROBERT M. SHARPE, Executors of the Last Will and Testament of DANIEL WILLIAMS FARNSWORTH, Deceased,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITIONS FOR REVIEW OF DECISIONS OF THE TAX COURT OF THE UNITED STATES

Argued December 18, 1958

Reargued June 11, 1959

Before: BIGGS, Chief Judge, and MCLAUGHLIN and HASTIE, Circuit Judges.

By Biggs, Chief Judge:

In these cases the petitioners-taxpayers, the executors of the decedent Farnsworth,[1] the senior or managing partner in a series of partnerships styled "Farnsworth & Farnsworth" over a number of years, seek to deduct from Farnsworth's federal income tax bases for the years 1952 and 1953 amounts paid by him to the State of New York by way of compromise of claims asserted by the New York State Tax Commission for taxes due from the partnerships under the Unincorporated Business Tax Law of New York, 59 McKinney's Laws of New York, Section 386 *et seq.*, and sums paid by Farnsworth by way of compromise of individual income tax claims asserted by the State of New York against him and his partners, 59 McKinney's Laws of New York, Section 350 *et seq.*

The Farnsworth partnerships and Farnsworth and his partners did not pay New York taxes despite the fact that the partnerships as consultants for woolen mills did some business in New York and at least one of the partners in one of the successive partnerships lived there. Farnsworth, being informed of probable New York tax liability by his counsel, filed partnership returns with the New York State Tax Commission which showed substantial tax liabilities. These returns were audited by the Commissioner and the amounts due were increased by interest and penalties. Tax liens in favor of the State of New York were filed against the partnerships and against the individual partners in New York. After considerable negotiation the New York tax authorities agreed to compromise all tax liabilities if confessions of judgment for personal and partnership taxes, which would be enforceable in every State, were procured from Farnsworth and his partners.

Thereafter, at a meeting at his home in Montclair, New Jersey, on April 24, 1952, Farnsworth, then eighty-six

[1] The taxpayer, Daniel W. Farnsworth, died of a heart attack on September 25, 1958. His executors, Gertrude Adams Farnsworth, James D. Carpenter, and Robert M. Sharpe, by order of the Tax Court dated October 16, 1958, were substituted as petitioners in his stead. The taxpayer's wife signed joint returns.

years of age and suffering from a heart attack, and greatly troubled by the hard tax situation confronting himself, his partnerships, and his partners, some of whom were related to him by blood or marriage, stated that he would assume all New York tax liability of the partnerships and of the individual partners if the individual partners would cooperate by executing confessions of judgment as required by New York. It is conceded that Farnsworth waived his right to contribution from his partners, if any, for the payments made or to be made by him on their behalf. A compromise agreement with New York was executed by all the partners[2] and Farnsworth and his partners executed the required confessions of judgment which were entered against them. Thereafter Farnsworth paid in instalments the full amount of the compromise which embraced all partnership and individual tax liability. As we have said, the Tax Court refused to permit these deductions in gross but did, however, allow Farnsworth to deduct the sums paid by him by way of compromise of his own New York State income tax liability and also permitted him to deduct his aliquot portion of the sums paid by him in compromising the partnership liabilities due under the Unincorporated Business Tax Law of New York. See 29 T.C. 1131 (1958).

Farnsworth's executors contend that his estate is entitled to take as deductions all the sums paid by him pursuant to Section 23(a)(1)(A) or Section 23(c)(1)[3] of the Internal Revenue Act of 1939, 26 U.S.C.A. (I.R.C. 1939) § 23. The Commissioner not only disputes the applicability of these two sections but argues that even if the sums paid

[2] See Exhibit 21.

[3] "§ 23. Deductions from gross income. In computing net income there shall be allowed as deductions:

"(a) (1) (A) All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business. . . .

"(c) Taxes generally.

"(1) Allowance in general. Taxes paid or accrued within the taxable year. . . ."

could be taken as deductions ordinarily, nonetheless Section 385 of the New York tax law, 59 McKinney's Laws of New York § 385, prevents the taxpayers, Farnsworth's executors, from deducting the amounts paid by him by way of compromise of either his partners' personal income taxes or of the partnerships', unincorporated business taxes. Section 385 forbids any person from directly or indirectly contracting to pay another's personal taxes, and provides that any such contract will be null, void and unenforceable.[4] [5] The Commissioner contends that Farnsworth's agreement to pay the State personal income taxes of his partners is illegal, void and unenforceable under New York law. He contends next that under *Di Raimondo* v. *Lembo*, 63 N. Y. S. 2d 906 (1946), the agreement made by Farnsworth to compromise the partnerships' taxes is also void as against the public policy of the State of New York despite the fact that Farnsworth was individually liable for all of the partnership taxes as was every other member of the partnerships under the law of New York, 38 McKinney's Laws of New York, Section 26. The Commissioner contends that since the agreement concerning the compromise of both the personal and the partnership taxes was embodied in a single document the agreement of Farnsworth to compromise the partnership taxes, for which he was liable, was contaminated by Farnsworth's agreement to pay his partners' individual New York income tax liabilities. The Commissioner does not contend, and logically cannot contend, that the payment by Farnsworth of his own individual income taxes was against public policy.

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[4] 59 McKinney § 385, provides: "It shall be unlawful for any person to agree or contract directly or indirectly to pay or assume or bear the burden of any tax payable by any taxpayer under the provisions of this Article [i.e. personal income taxes]. Any such contract or agreement shall be null and void and shall not be enforced or given effect by any court."

[5] The issue of frustration of State policy was first raised by this court *sua sponte*. Reargument was granted because of it and the parties ably argued orally and on their briefs the issue suggested as pertinent by the court.

The Commissioner argues that under the doctrine most recently expressed in *Tank Truck Rentals, Inc.* v. *Commissioner*, 356 U.S. 30 (1958), and *Hoover Express Co.* v. *United States*, 356 U.S. 38 (1958), deductions will not be permitted from federal income taxes when the allowance of such deductions will contravene a sharply defined State public policy. Therefore, argues the Commissioner, permitting a deduction for another partner's personal income tax would undermine New York's sharply defined public policy, and consequently we may not permit the deductions sought by Farnsworth in respect to the payments made by him to settle his partners' and partnerships' tax liabilities.

Farnsworth's executors, the taxpayers, argue that the compromise agreement made and subsequently executed by Farnsworth with his partners for the settlement of all New York tax liabilities is to be construed by New Jersey law and thus Section 385 of the New York Tax Code is inapplicable, and furthermore that even if New York law be deemed to be applicable the assumption of settlement of the partnership taxes by Farnsworth may be severed from the assumption of settlement by Farnsworth of his partners' personal taxes, and that in any case the policy expressed in Section 385 is not such as to require protection by denying federal income tax deductions.

We can perceive no question of conflict of laws presented by the facts at bar. The issues presented must be resolved by federal law since federal tax issues are involved. If the circumstances presently presented are such as to contravene the public policy of New York within the ruling of Tank Truck Rentals, Inc., in our opinion it would make no difference as to where the compromise agreement was entered into or where it was executed. The tax law of the United States is uniform and is the same in New Jersey as it is in New York and throughout the United States.

The New York State Tax Commission conditioned settlement upon the execution of confessions of judgment for the personal income taxes of Farnsworth's partners

and for the partnerships' New York unincorporated business taxes as well. Farnsworth's liability also was required to be covered by a confession of judgment. On this record, however, it does not appear affirmatively that the New York State Tax Commission was aware that Farnsworth made himself liable for the compromise of all the tax liabilities. Nor does it appear, despite the fact that Farnsworth made the payments by his own personal checks and signed some of the confessions of judgment which also were signed by other individual partners, that the New York State Tax Commission knew that he was making these payments from his own funds *solus* and waiving his right of contribution from his partners. Section 385 is not a criminal, a quasi-criminal, or even a penalty statute. Its sanctions are purely civil, i.e., the denial of enforcement of contracts made contrary to its provisions.[6] In the *Tank Truck Rentals, Inc.* case the Supreme Court held that fines for violation of State maximum weight laws were not deductible as ordinary and necessary business expenses under Section 23(a)(1)(A) of the Internal Revenue Code of 1939, 26 U. S. C. A. § 23(a)(1)(A), and that to allow the deductions would frustrate State policies proscribing particular types of conduct evidenced by State Law. Here the deductions are sought by Farnsworth under Section 23(a)(1)(A) and Section 23(c)(1) of the Internal Revenue Code of 1939, 26 U. S. C. A. §§ 23(a)(1)(A), 23(c)(1).

We can perceive no substantial basis for making a distinction in respect to the federal statute under which the deduction is sought to be allowed and none in the fact that Farnsworth acted apparently in innocent contravention of the New York statute. *Hoover Express Co.* v.

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[6] The precise motivation of Section 385 is difficult to ascertain. There seems to be no available legislative history. However, it is interesting to note that many states recognize as legal covenants to pay other's income taxes. See e.g. Young v. Illinois, 310 Ill. 75, 141 N. E. 369; Republic Bldg. v. Goestner, 201 Ky. 509, 256 S. W. 1111; Kimball v. Cotting, 229 Mass. 541, 118 N. E. 866. It is possible that the intent of the New York State Legislature in enacting Section 385 was merely to prevent collusive or otherwise illegal agreements in respect to divorce proceedings.

United States, supra. It appears, however, that the doctrine of contravention of a State revenue statute set out in *Textile Mills Securities Corporation* v. *Commissioner*, 314 U. S. 326 (1941) and *Commissioner* v. *Heininger*, 320 U.S. 467, 473 (1943), was intended to be and is shown to be a limited one by the decisions in Tank Truck Rentals, Inc. and Hoover. Tank Truck Rentals, Inc. teaches that each case must turn on its own facts and that the test of non-deductibility always lies in the severity and immediacy of the frustration which would result to the State from the allowance of the federal deduction. Under Section 385 payment is not a statutory violation. The contract for the payment is merely rendered unenforceable. Here, the compromise agreement was executed fully. This is not a minor distinction in view of the fact that the New York *fisc* was not frustrated for it received the funds for which it contracted by way of the compromise agreement. The purpose behind the New York State statute is unclear, to say the least. We have found no decision and none has been cited to us which applies the doctrine of frustration to statutes purely civil in their nature. Absent an express ruling by the Supreme Court on this issue, we are of the opinion that the tendency of that Court is to limit the effect of the frustration doctrine and we state it as our view, upon consideration and examination of the cases, that the Supreme Court would not apply the doctrine of *Textile Mills Securities Corporation* v. *Commissioner* and similar authorities, under the circumstances of the case at bar, to deprive Farnsworth's estate of the benefit of deductions specifically provided for by the federal income tax statutes.

We must determine next if any provisions of the 1939 Tax Code permit the deductions in issue. In this connection we deal first with all of the deductions sought without regard to whether they are sought under Section 23(c)(1) or Sections 23(a)(1)(A). We will discuss the applicability of the two sections referred to at a later point in this opinion. Farnsworth argues that by oral modifications of the partnership agreements, effected *post* the discovery by him and his partners of the New York State tax liabilities he made himself solely liable for those liabilities and there-

fore should be permitted to deduct the payments made by him by way of compromise from his federal income taxes in the years in question. That Farnsworth did undertake to make himself so liable and did not exact any contribution or reimbursement from his partners for their shares of the sums paid by way of compromise of the tax liabilities cannot be disputed. But the Commissioner ruled and the Tax Court in effect found that the assumption of liability, any payment of the sums required by the compromise by Farnsworth and his waiver of his right to contribution from and reimbursement by his partners constituted a mere gift and was not supported by valid consideration.

Farnsworth's executors' position is of course to the contrary and can be summed up as follows. They assert and Farnsworth asserted at the trial that he could not do business in New York unless all tax liabilities, his own, those of his partners and those of the partnership were paid or compromised.[7] Farnsworth testified that the New York State Tax Commission was unwilling to settle or dispose of any tax liability unless all tax liabilities were compromised. But if all tax liabilities were compromised the Commission was willing to permit installment payments. It was his evidence that to get his partners to agree to the compromise and to execute confessions of judgment he had to agree to waive his right to contribution from or reimbursement by his partners for they hotly contested all of the New York tax claims.[8] Farnsworth's counsel who engineered the compromise agreement with the New York State Tax Commission strongly supported the evidence given by Farnsworth in these respects by his testimony.

[7] When asked what would have been the effect on his partnerships or partnerships of non-settlement of the New York tax liabilities Farnsworth replied: "Rather disastrous."

When asked what would have been the effect on the business of the partnerships if all tax liability had had to be paid "at one lump", Farnsworth replied: "It would ruin them."

[8] Only two partners apparently did not object to paying or compromising their respective New York State tax liabilities. One was Peter Egan who lived in New Jersey. The other was James Hastie, the partner resident in New York. The compromise agreement covered all partners in all of the partnerships existent at the critical dates and also all partnerships involved in New York tax liabilities

Ergo, say the taxpayers, Farnsworth, cast upon the horns of this dilemma, was compelled to compromise all tax liabilities at his own expense.

In respect to these issues the Tax Court stated "It is, to be sure, contended that petitioner could not settle his own liability for the taxes in question without disposing of all of the New York State claims in one arrangement and that his ex-partners were unwilling to concede their liability. But as the case is presented, we are unable to find that any defense the ex-partners may have had would have been effective, nor indeed that it was necessary for petitioner to relinquish his rights of contribution had he made the settlement by paying the entire amount and seeking to recover from the ex-partners."

That Farnsworth could not do business in New York unless the income taxes arising under the New York Unincorporated Business Tax Law due from him were paid or compromised is a self-evident and necessary inference which this court is entitled to draw. Any business accounts which accrued to Farnsworth's advantage in New York could have been garnished by that State and he also would have been subject to criminal penalties as well. See 59 McKinney's Laws of New York, Section 376. But we cannot infer from the record that Farnsworth could not effect the compromise unless he undertook personally to pay the sums required by the compromise without contributions from or reimbursements by his partners. The Tax Court in effect found against the taxpayers on this issue, or at least made no finding or conclusion supporting their assertion in this regard. The obstacle to deciding in Farnsworth's executors' favor on this issue lies in the fact that we cannot hold on consideration of the whole of the records the result reached by the Tax Court was clearly erroneous. We have scrutinized the testimony in these cases and all of the documentary evidence. We shall not discuss the records or detail Farnsworth's own statements but the latter do afford a basis whereby the Tax Court was entitled to conclude that Farnsworth's mind was, to employ his own words, "fixed to settle it and get the whole thing off the slate," and that he felt himself bound by a moral obligation

as the chief partner to wipe out the tax liabilities of his partners and the partnerships. It must be borne in mind also that there were strong familial reasons for Farnsworth to do this. Some of his partners were related to him by blood and marriage and many of them had been in business with him for years. We cannot say that the Tax Court was clearly in error in concluding that Farnsworth was not compelled to settle *solus* all tax liabilities of his partners and his partnerships in order to conduct or maintain his business in New York.

It follows that Farnsworth's executors are not entitled to the deductions sought by them under Section 23(c)(1) as taxes paid or accrued within the taxable years for Farnsworth gratuitously assumed full liability without contribution or reimbursement for the payment of the compromise of the New York State tax liabilities and therefore the payments made by him are not deductible. We point out also that sums paid by way of taxes are deductible only by the person upon whom the taxes are imposed except under special circumstances not present here. See *Magruder* v. *Supplee*, 316 U. S. 394, 396 (1942), quoting Article 23(c)-1 of Treasury Regulations 94. Specifically as to the partnerships' New York tax liability since the Tax Court failed to find or conclude that Farnsworth had to waive contribution from his partners in order to effect the settlement but did this gratuitously, his executors are entitled to deduct only his aliquot share of the sums paid by him in compromise of the partnership tax liabilities.

Section 23(a)(1)(A) cannot afford a basis for the deductions since the obligations were found by the Tax Court to be gratuitously assumed by Farnsworth and therefore the payments made by him in settlement of them did not constitute a business necessity.

The decisions of the Tax Court will be affirmed.

A True Copy:

Teste:

Clerk of the United States Court of Appeals for the Third Circuit.

III.

Provisions of the Internal Revenue Code of 1939 affecting this case.

[Sec. 23(c)]

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

* * * * * *

(c) TAXES GENERALLY.—

(1) ALLOWANCE IN GENERAL.—Taxes paid or accrued within the taxable year, except—

(none of the exceptions are relevant here)

* * * * * *

SEC. 181. PARTNERSHIP NOT TAXABLE.

Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity.

SEC. 182. TAX OF PARTNERS.

In computing the net income of each partner, he shall include, whether or not distribution is made to him—

* * * * * *

(c) His distributive share of the ordinary net income or the ordinary net loss of the partnership, computed as provided in section 183(b).

SEC. 183. COMPUTATION OF PARTNERSHIP INCOME.

(a) GENERAL RULE.—The net income of the partnership shall be computed in the same manner and on the same basis as in the case of an individual, except as provided in subsections (b), (c), and (d).

(b) SEGREGATION OF ITEMS.—

(1) CAPITAL GAINS AND LOSSES.—There shall be segregated the gains and losses from sales or exchanges of capital assets.

(2) ORDINARY NET INCOME OR LOSS.—After excluding all items of gain and loss from sales or exchanges of capital assets, there shall be computed—

(A) An ordinary net income which shall consist of the excess of the gross income over the deductions; or

(B) An ordinary net loss which shall consist of the excess of the deductions over the gross income.

* * * * * *

SEC. 187. PARTNERSHIP RETURNS.

Every partnership shall make a return for each taxable year, stating specifically the items of its gross income and the deductions allowed by this chapter and such other information for the purpose of carrying out the provisions of this chapter as the Commissioner with the approval of the Secretary may by regulations prescribe, and shall include in the return the names and addresses of the individuals who would be entitled to share in the net income if distributed and the amount of the distributive share of each individual. The return shall be sworn to by any one of the partners.

* * * * * *

SEC. 189. NET OPERATING LOSSES.

The benefit of the deduction for net operating losses allowed by section 23 (s) shall not be allowed to a partnership but shall be allowed to the members of the partnership under regulations prescribed by the Commissioner with the approval of the Secretary.

* * * * * *

IV.

Provisions of Income Tax Regulations 118* Affecting This Case.

§ 39.23 (c)-1 TAXES.

(a) In general. Subject to the exceptions stated in this section and §§ 39.23 (c)-2 and 39.23 (c)-3, taxes imposed by the United States, any State or Territory, or political subdivision of either possessions of the United States, or foreign countries, are deductible from gross income for the year in which paid or accrued (see section 43). Estate, inheritance, legacy, succession, and gift taxes, the employment taxes imposed by sections 1400, 1600, and 1510, and Federal income taxes (including the tax withheld at source under section 1622) are not deductible from gross income. The Federal war-profits and excess-profits taxes imposed by Title II of the Revenue Act of 1917, Title III of the Revenue Act of 1918, Title III of the Revenue Act of 1921, section 216 of the National Industrial Recovery Act, section 702 of the Revenue Act of 1934, and subchapter E of chapter 2 are not deductible from gross income. Income, war-profits, and excess-profits taxes imposed by the authority of any foreign country or possession of the United States are deductible from gross income in cases where the taxpayer does not choose to take to any extent for the taxable year the benefits of section 131 (relating to credit for taxes of foreign countries or possessions of the United States). See the last sentence of section 131 (a). Postage is not a tax. Amounts paid to States or Territories under security debts laws in order to render securities tax exempt are deductible. Automobile license fees are ordinarily taxes. In general taxes are deductible only by the person upon whom they are imposed. As to tax paid at the source on interest from tax-free covenant bonds, see section 143 (a)(3).

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*NOTE: These Regulations, although promulgated September 26, 1933 are by their own terms retroactive to January 1, 1932. Regulations 118, Section 39.1-1(b)

§ 39.181-1 PARTNERSHIPS.

Partnerships as such are not subject to the income tax imposed by chapter 1, but are required to make returns of income. See sections 187 and 188. For definition of what the term "partnership" includes, see section 3797 (a)(2). For rules as to allocation of partnership income in the case of family partnerships, see section 191 of the regulations thereunder.

§ 39.182-1 DISTRIBUTIVE SHARES OF PARTNERS.

(a) Each partner is required to include in his return for his taxable year within which or with which the taxable year of the partnership ends, whether or not distributed:

* * * * * * *

(3) His distributive share of the ordinary net income or the ordinary net loss of the partnership, computed as provided in section 183 (b).

* * * * * * *

§ 39.183-1. COMPUTATION OF PARTNERSHIP INCOME.

The net income of the partnership shall be computed in the same manner and on the same basis as the net income of an individual, except that:

(a) The partnership is required to segregate its gains and losses from sales or exchanges of capital assets. A partnership is not allowed the benefit of section 117 (e).

(b) The partnership is further required, after excluding all items described in paragraph (a) of this section, to compute (1) an ordinary net income which consists of the excess of gross income over the deductions, or (2) an ordinary net loss which consists of the excess of the deductions over the gross income. In the computation of its ordinary net income or ordinary net loss, the partnership is denied the so-called charitable contribution deduction

allowed by section 23(o), but each partner is considered as having made payment, within his taxable year, of his distributive portion of any contribution or gift, payment of which was made by the partnership within its taxable year, of a character which would be allowed to the partnership as a deduction if section 183(c) had not been enacted. Payments made to a partner for services rendered and for interest on capital contributions are not deductible in computing the net income of the partnership, such payments being held to represent a division of partnership profits.

* * * * * *

39.187-1 Partnership Returns.

Every partnership shall make a return of income, regardless of the amount of its net income (see section 3797(a) (2), defining the term "partnership"). The return shall be on Form 1065; shall state specifically the information required to be stated by the return form; shall be filled in according to the instructions contained thereon or issued with respect thereto; and shall contain or be verified by a written declaration, signed by one of the partners, that it is made under the penalties of perjury. Such return shall be made for the taxable year of the partnership, that is, for its annual accounting period (fiscal year or calendar year, as the case may be), irrespective of the taxable years of the partners. See sections 182 and 183. If the partnership makes any change in its accounting period, it shall make its return in accordance with the provisions of section 47, except that the return shall not be placed on an annual basis under section 47(c).

39.189-1 Net Operating Loss Deduction in the Case of Partners.

(a) In General. The benefit of the deduction for net operating losses provided by section 23(s) shall not be allowed to a partnership. In computing his own net operating loss or his own net income (where required to be

computed in accordance with the exceptions and limitations provided in section 122(d) (1) to (4), inclusive) for any taxable year for the purposes of the computations required by section 122, however, each partner shall take into account the income and losses of the partnership in accordance with sections 182 to 188, inclusive, with the exceptions and limitations set forth in paragraphs (b) and (c) of this section.

* * * * * *

(3) Ordinary net income or loss. (i) After excluding all items required to be segregated by subparagraphs (1) and (2) of this paragraph, there shall be computed—

(a) A business ordinary net income of the partnership, which shall consist of the excess of the business gross income over the business deductions; or

(b) A business ordinary net loss of the partnership, which shall consist of the excess of the business deductions over the business gross income; and

(c) A nonbusiness ordinary net income of the partnership, which shall consist of the excess of the nonbusiness gross income over the nonbusiness deductions; or

(d) A nonbusiness ordinary net loss of the partnership, which shall consist of the excess of the nonbusiness deductions over the nonbusiness gross income.

In making the move computations the limitations and exceptions provided by section 122(d) (1) and (2) shall be applied.

(ii) His distributive share of a business ordinary net income of the partnership shall be included by each partner as ordinary business gross income, and of a business ordinary net loss of the partnership as an ordinary business deduction. His distributive share of a nonbusiness ordinary net income of the partnership shall be included by each partner as ordinary nonbusiness gross income, and of a nonbusiness ordinary net loss of the partnership as an ordinary nonbusiness deduction.

(c) Exceptions and limitations applicable in computation of partner's net income. (1) The ordinary net income or ordinary net loss of the partnership shall be computed with the exceptions and limitations provided in section 122 (d) (1) and (2).

(2) The partnership's gains and losses from sales or exchanges of capital assets held for more than six months shall be taken in account in full.

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V.

Settlement Agreement, Exhibit 21-U, and Excerpt from Schedule A Attached Thereto.

November 28, 1952.

Hon. Spencer E. Bates
State Tax Commission
State Office Building
Albany 1, New York.

Re: Farnsworth and Farnsworth.

Dear Sir:

At conferences held with our attorneys, attended by yourself, Commissioner Goodrich, and other representatives of the State Tax Commission, a tentative agreement was reached concerning the manner in which disposition is to be made of the tax liabilities of the above partnership and its member partners, under Articles 16 and 16-A of the New York Tax Law, and such tax liabilities satisfied.

Such agreement, which the undersigned hereby ratify and approve, is as follows:

1. Assessments of additional tax have heretofore been issued against the partnership of Farnsworth and Farnsworth, for the unincorporated business income taxes imposed by Article 16-A of the Tax Law, in the total amount of $42,410.77, and against the undersigned individual member partners for personal income taxes imposed by Article 16 of the Tax Law, in the total amount of $46,944.95, together with statutory penalties and interest to July 15, 1951, as set forth in Schedule A, annexed hereto. Each of the undersigned individuals acknowledges liability for his or her respective personal income taxes and penalties and interest with respect thereto set forth opposite his or her name in Schedule A, and all of the undersigned acknowledge their liability for the unincorporated business income taxes, penalties, and interest to the extent

applicable to the years during which they were respectively members of the partnership of Farnsworth and Farnsworth, as set forth in Schedule A. The foregoing acknowledgements are in no way to be construed as an admission of fraud or bad faith with respect to the taxes which are the subject of this agreement, but are made for the purpose of this agreement only.

2. In the manner hereinafter set forth, with interest at the rate of 6% per annum from the original due date of each tax, (a) each of the undersigned individuals agrees to pay the personal income taxes set forth opposite his or her respective name in Schedule A, and (b) all of the undersigned agree to pay the unincorporated business income taxes to the extent applicable to the years during which they were respectively members of the partnership of Farnsworth and Farnsworth as set forth in Schedule A.

3. In part payment of such indebtedness, there is herewith submitted a certified check payable to the State Tax Commission, made by Farnsworth and Farnsworth, drawn upon the Montclair Trust Company, in the amount of $40,053.98. The proceeds of such check are to applied, tentatively and subject to the provisions of Paragraph 8 of this agreement, (a) to the extent of $8,900, against the earliest accrued personal income taxes owing by Daniel Farnsworth, and (b) to the extent of the balance of $31,153.98, against the earliest accrued unincorporated business income taxes owing by the partnership. It is understood that for the purposes of computation of interest under this agreement, payment of the aforesaid amount of $40,053.98 shall be considered to be effective as of the date of said check, to wit, June 2, 1952.

4. The remainder of the unincorporated business income taxes in the amount of $11,256.79, together with the interest then due as to said unincorporated business income taxes in the amount of $8,226.46, making a total of $19,483.25, shall be paid to the State Tax Commission on or before February 15, 1953, as set forth in Schedules

B and B-1. As computed in Schedule B-1, the amount of interest otherwise payable has been reduced by the proportionate part of the unincorporated business income taxes allocable to Frederick C. Farnsworth and Claribel C. Farnsworth, deceased members of the partnership, and the amount of the reduction applied in payment of the unincorporated business income taxes allocable to Claribel C. Farnsworth, deceased, and Frederick C. Farnsworth, deceased.

There shall also be paid to the State Tax Commission, on or before February 15, 1953, one-half of the balance of the personal income taxes, exclusive of interest, herein agreed to be paid by the individual member partners (not including Frederick C. Farnsworth, deceased, and Claribel C. Farnsworth, deceased) in the total amount of $19,019.52, such payment to be proportionately credited against the earliest accruing tax liabilities of such individuals, as set forth in Schedules C and C-1, subject to the provisions of Paragraph 8 of this agreement.

5. The remainder of the personal income taxes agreed to be paid by said individual member partners, together with all interest due on said personal income taxes, less credit of interest on the payments of said personal income taxes theretofore made, in the total amount of $37,385.59, is to be paid to the State Tax Commission on or before February 15, 1954, as set forth in Schedules C and C-1.

6. The statutory penalties and interest assessed with respect to the unincorporated business income taxes shall be abated, and all liability of the undersigned individuals for said taxes, penalties, and interest shall cease with and be discharged only upon completion of payment of the taxes and interest, as provided in Paragraphs 3, 4, and 5 above.

The statutory penalties and interest assessed with respect to the personal income tax liability of each of the undersigned individuals shall be abated, and all liability of such individual for personal income taxes, penalties, and interest hereunder shall cease with and be discharged only

by the completion of payment of the personal income taxes and interest agreed by such individuals to be paid under this agreement. It is further provided that any of the undersigned individuals may individually, at any time, and from time to time, make payment to the State Tax Commission on account of his or her respective personal income tax liability and interest due thereon, and such payments shall be credited against the payments otherwise due with respect to such individual or on before February 15, 1953, as provided in the second part of Paragraph 4 above, and on or before February 15, 1954, as provided in Paragraph 5 above.

7. It is a condition of this agreement that there shall be deposited with the State Tax Commission, within thirty days from the execution of this agreement, the following confessions of judgment, to be held by the State Tax Commission only as security for the payments herein agreed to be made and subject to the following terms and conditions:

a. Confessions of judgment in favor of the State Tax Commission of the State of New York, for the tax years referred to in Schedule A, signed by each of the undersigned who was a partner in Farnsworth and Farnsworth during the year or years covered by the confession of judgment. Such confessions of judgment shall be in the total amount of $60,233.34, representing the unincorporated business income taxes in the amount of $42,410.77, together with interest at the rate of 6% per annum to February 15, 1953 in the amount of $17,822.59. Such confessions of judgment are to be held by the State Tax Commission, subject to the provisions of Paragraph 8 of this agreement, only as security for the payment of unincorporated business income taxes and interest thereon agreed to be made on or before February 15, 1953, and will be returned to the partnership, or its attorneys, upon completion of such payments in accordance with the provisions of Paragraph 4 above. However, in the event of any default in payment, the State Tax Commission is hereby authorized to file such confessions of judgment in the State of New Jersey and to proceed

to enforce the collection thereof by all available means. Such confessions of judgment shall be prepared and executed in accordance with the applicable laws of the State of New Jersey, and shall be in the proper form for filing in the designated court of such state.

b. In the case of each of the following individuals, a confession of judgment in favor of the State Tax Commission of the State of New York for such individual's personal income taxes, together with interest at the rate of 6% per annum to February 15, 1953, as follows:

Peter J. Egan	$ 4,171.22
Janet C. Emslie	5,289.33
Daniel W. Farnsworth	12,555.34
Josephine Farnsworth	6,931.75
A. Louise Gordon	5,820.18
Frances F. Jaeckel	6,428.60
Helen F. Schneidewind	6,243.93
Howard B. Schneidewind	8,550.70
Robert M. Sharpe	2,862.80
Claribel F. Sulzberger	6,044.24

Each such confession of judgment is to be held by the State Tax Commission, subject to the provisions of Paragraph 8 of this agreement, only as security for the payments of personal income taxes and interest thereon agreed to be made by each such individual, and will be returned to such individual, or his or her attorneys, upon completion of such individual's payments, in accordance with the provisions of this agreement. In the event of any default in payment, the State Tax Commission is hereby authorized to file such confession of judgment in the state of legal residence of the individual, and to proceed to enforce collection thereof by all available means. Each such confession of judgment shall be prepared and executed in accordance with the applicable laws of the individual's respective state of legal residence, and shall be in proper form for filing in the designated court of such state.

8. Any other provision of this agreement notwithstanding, it is specifically understood and agreed as follows:

a. In the event of a default in payment of all or any part of the second installment due hereunder, to wit the sum of $38,502.77 agreed to be paid on or before February 15, 1953 as provided in Paragraph 4 of this agreement, the full amount of unincorporated business income taxes, personal income taxes, statutory penalties and interest previously assessed against the undersigned individuals and the firm of Farnsworth & Farnsworth as set forth in Schedule A shall forthwith become due and payable, and the sum of $40,053.98 referred to in Paragraph 3 above and paid to the State Tax Commission upon the execution of this agreement shall not be regarded as paid on account of the basic unincorporated business income taxes and personal income taxes owing by Daniel Farnsworth, but shall be applied against the statutory penalties and interest due with respect to said unincorporated business income taxes as set forth in Schedule A.

b. In the even of any default in payment of or on account of the personal income tax liability and interest thereon agreed to be paid with respect to any of the undersigned individuals on or before February 15, 1954 as provided in Paragraph 5 of this agreement, there shall immediately be due and payable as to such individual (and such individual only) the entire amount of the personal income taxes, statutory penalties and interest previously assessed against such individual as set forth in Schedule A, and all previous payments representing personal income taxes and interest thereon made by or for the account of said individual pursuant to Paragraphs 3 and 4 of this agreement shall not be regarded as paid on account of such individual's basic personal income tax liability but shall be applied against the statutory penalties and interest due with respect to such individual.

9. Your signature, or the signature of any other Tax Commissioner or Deputy Tax Commissioner, on the accom-

panying copy of this letter will acknowledge acceptance by the State Tax Commission of the terms of the agreement as above set forth.

Very truly yours,

PETER J. EGAN
PETER J. EGAN

JANET C. EMSLIE
JANET C. EMSLIE

DANIEL W. FARNSWORTH
DANIEL W. FARNSWORTH

JOSEPHINE FARNSWORTH
by Janet C. Emslie, attorney in fact
JOSEPHINE FARNSWORTH

A. LOUISE GORDON
A. LOUISE GORDON

JAMES H. HASTIE
JAMES H. HASTIE

FRANCES F. JAECKEL
FRANCES F. JAECKEL

HELEN F. SCHNEIDEWIND
HELEN F. SCHNEIDEWIND

HOWARD B. SCHNEIDEWIND
HOWARD B. SCHNEIDEWIND

ROBERT M. SHARPE
ROBERT M. SHARPE

CLARIBEL F. SULZBERGER
CLARIBEL F. SULZBERGER

Samuel Rosenblatt—

individually and as member partners of the partnership of Farnsworth and Farnsworth.

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Excerpt from Schedule A.

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Taxpayer	Assessment No.	Tax Year	Tax	P & I	Total
Farnsworth and Farnsworth	FA 24782	11/30/40	1,178.43	4,100.93	5,279.36
	24783	11/30/41	3,039.42	9,846.42	12,885.44
	24784	11/30/42	3,560.97	10,682.91	14,243.88
	24785	11/30/43	4,252.82	11,737.85	15,990.67
	24786	11/30/44	7,232.04	18,224.77	25,456.81
	24787	11/30/44	5,623.34	12,821.22	18,444.56
	24788	11/30/46	7,167.28	14,617.17	21,782.45
	24789	11/30/47	1,518.55	2,733.39	4,251.94
	24790	11/30/48	4,796.69	7,482.84	12,279.53
	24791	11/30/49	4,043.63	5,337.59	9,381.22
			$42,410.77	$97,585.09	$139,995.86